FILED
JAN 22 2008
OFFICE OF THE CLERK
SUPREME COURT, U.S.

(3)

07-775

No. [redacted]

IN THE

# Supreme Court of the United States

**ALLSTATE INSURANCE COMPANY** and
**STERLING COLLISION CENTERS, INC.,**
*Petitioners,*

v.

**GREGG ABBOTT,**
in his Official Capacity as Attorney General of Texas, and
**SUSAN COMBS,**
in her Official Capacity as Texas Comptroller of Public Accounts,
*Respondents,*

v.

**AUTOMOTIVE SERVICE ASSOCIATION** and
**CONSUMER CHOICE IN AUTOBODY REPAIR,**
*Respondents/Intervenors.*

**On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit**

## REPLY BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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January 22, 2008

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D.C. 20002

## RULE 29.6 STATEMENT

The corporate disclosure statement included in the petition for a writ of certiorari remains accurate.

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## REPLY BRIEF FOR PETITIONERS

Allstate's Petition demonstrated the urgent need for this Court's review of a widening lower court split over state power to "protect the local independent folks back home" from innovative, interstate competition. As Allstate showed, the Fifth Circuit departed from this Court's settled Commerce Clause jurisprudence, establishing a dangerous precedent giving States enhanced power to pass protectionist legislation.

Implicitly acknowledging that the challenged statute primarily protects the profits and dominance of local Texas body shops at the expense of Texas consumers, the State of Texas waived its right to file a response. The only response came from the Intervenor lobbyists, the corporeal embodiment of the "local folks back home" protected by HB 1131. This is unsurprising. From the outset, the local Texas body shop owners – and their well-heeled lobbyists – have been the impetus for HB 1131, drafting and hawking it, pushing their friendly legislators to act, and leading its defense at trial and on appeal.

Intervenors do not deny that States are increasingly enacting anti-vertical integration, "anti-Wal-Mart-type legislation" to prevent new business models from shifting sales away from local enterprises. Nor do they deny that the Fifth Circuit's approach gives States carte blanche to enact such protectionist legislation. Their principal argument invokes anti-insurer bias. They claim that this case is about insurance regulation. Opp. 2.

Not so. Neither court below bought that ruse. Specifically rejecting Intervenors' McCarran-Ferguson Act ("MFA") argument, the district court recognized that HB 1131 regulates the business of collision repair (not insurance); the Fifth Circuit did not even address the issue. Nothing else in Intervenors' response should deter this Court from granting *certiorari* to vindicate the principles undergirding our national economic union. The Fifth Circuit's deferential stance is misguided federalism at its worst.

## 1. Intervenors' MFA Argument Is An Irrelevant Diversion.

Intervenors' MFA argument is both procedurally and substantively flawed. Procedurally, both courts below rejected the MFA defense. Intervenors have not cross-petitioned on MFA (or any other) grounds. Intervenors essentially ask this Court to assume that the courts below erred in not accepting their MFA argument. This is improper.

Intervenors claim that, given the MFA, *Spector Motor Service v. McLaughlin*, 323 U.S. 101, 105 (1994), shows this is not a "good" case to address the important Commerce Clause issues. Opp. 3, 8. Their argument misses the mark. *Spector* is a ripeness case. No ripeness issue is advanced here. With an elaborately developed factual record, this case presents an attractive vehicle for resolution of issues vital to the conduct of commerce across state borders.

Substantively, Intervenors' MFA argument was rightly dismissed by the district court because HB

1131 regulates the business of collision repair, not insurance. App. 68a-75a. As this Court has held, the MFA "did not purport to make the States supreme in regulating all the activities of insurance companies." *SEC v. Nat'l Sec., Inc.*, 393 U.S. 453, 459-60 (1969). "Insurance companies may do many things," but "only when they are engaged in the 'business of insurance' does the statute apply." *Id.*

The lower courts' rejection of the MFA defense correctly applied this Court's holding in *Group Life & Health Ins. v. Royal Drug Co.*, 440 U.S. 205, 215 (1979), that vertical integration into non-insurance markets does not constitute the "business of insurance." While Intervenors baldly assert that *Royal Drug* does not control (because the Commerce Clause exemption in Section 2(a) is broader than the antitrust exemption in Section 2(b), *see* Opp. 9-10), the district court rightly rejected this argument, as have other circuits. As the Sixth Circuit observed, the "Supreme Court ... assuredly did not give 'business of insurance' one meaning in the first clause and a different meaning in the second." *Owensboro Nat'l Bank v. Stephens*, 44 F.3d 388, 392 (6th Cir. 1994).

### 2. The Fifth Circuit's Disregard Of *Exxon's* "Business Shifting" Test Creates A Circuit Split.

The pivotal question is whether heightened scrutiny applies to laws that expressly "discriminate based not on domicile but on business form" and do so in substantial part to protect local companies from interstate competition. This question fundamentally implicates how much power States have to pass

protectionist, anti-vertical integration, anti-Wal-Mart-like legislation.

Intervenors assert this "is not a case about 'Anti-Wal-Mart legislation.'" Opp. 2. They are wrong. The Wal-Mart analogy was first raised, not by Allstate, but by Texas legislators seeking to protect local body shops from Sterling's entry. Representative Homer declared that nothing "angers me more than when the big guy comes in and just ... run[s] you out of town .... It's kind of the *Wal-Mart* scenario." App. 121a (emphasis added). Notwithstanding this (among other) evidence of protectionism, the Fifth Circuit held that heightened scrutiny does not apply because the State artfully discriminated based on "business form" (here, insurer ownership), not domicile.

Intervenors do not deny that the "business form" test conflicts with the "business shifting" test set forth in *Exxon v. Maryland*, 437 U.S. 117, 126 n.16 (1978). Nor do they deny that the Fifth Circuit's approach expands state power to enact protectionist measures. Instead, they assert that any form of anti-vertical integration legislation is constitutionally permissible because vertical integration is "potentially harmful to consumers or the markets." Opp. 3; *see also id.* 17 - 19.

As Allstate demonstrated, Pet. 11-23, the Fifth Circuit's "business form" exception cannot be reconciled with the many cases – including *Hunt v. Washington State Apple Advertising Comm.*, 432 U.S. 333 (1977); *Best & Co. v. Maxwell*, 311 U.S. 454 (1940); and *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984) – in which this Court invalidated facially-

neutral, "business form" discriminatory statutes. Intervenors make no attempt to distinguish *Hunt*, *Best*, or *Bacchus*, even though each of those cases applied heightened scrutiny to facially-neutral state laws that, like here, used "business form" distinctions to exclude targeted out-of-state rivals. *See* Pet. 13-15.

Intervenors claim that "[t]he Fifth Circuit did not create a *per se* rule that all laws regulating a 'business form' are immune from regulation." Opp. 11. This is a straw man. What a State may not do – unless there is a legitimate state purpose, sufficient to withstand heightened scrutiny – is prohibit a predominantly out-of-state business form to protect predominantly local businesses using a different business model.

The fallacy of Intervenors' argument is demonstrated by their own hypotheticals. Intervenors first assert, correctly, that if only in-state firms had sought to vertically integrate, HB 1131 would pose no problem under the Commerce Clause, since there would be no local protectionism. Intervenors then hypothesize that "the result should be no different" where, as here, the burdened class consists exclusively of out-of-state competitors. Opp. 14-15. This goes too far. Intervenors' rule would eviscerate the Commerce Clause's core value, as deprivation of "access to local demand" for out-of-state firms is the "essential vice" the Constitution guards against. *See C&A Carbone, Inc. v. Town of Clarkstown*, N.Y., 511 U.S. 383, 392 (1994).

Intervenors assert that the result below is compelled by *Exxon*. Opp. 17. Not so. As Allstate

explained, *Exxon* is factually distinguishable because the challenged Maryland statute had *no* effect on interstate commerce, as it did not shift *any* business from out-of-state firms to in-state competitors. Pet. 22-23; 437 U.S. at 126-27, n.16.

Intervenors claim that *Exxon* establishes *per se* validity for anti-vertical integration statutes. In their view, States may be "concern[ed] about an entity using its market power in one market to move into a separate market." Opp. 18-19. The proper question, however, is not whether States enacting anti-vertical integration statutes are "concerned" about adjacent market entry. They surely can be; indeed, virtually all States (including Texas) have antitrust laws to protect against "market power" exploitation.

The right question is: why is the State concerned? If the concern is that local businesses will suffer when out-of-state, vertically-integrated firms enter the market, then the law has a constitutionally impermissible purpose (and protectionist effect). *See* Pet. 12-14.[1]

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[1] Intervenors claim that insurer-ownership is an "anticompetitive business model." Opp. 3. The district court below properly found, however, that "[s]ince Sterling only holds about a 2% share of the Texas autobody repair market, this court doubts that Sterling's presence in the marketplace ... [has] resulted in unfair competition." App. 102a. Further, as the district court also noted, Texas has employed "less restrictive means of protecting consumers and fair competition in the marketplace" by way of an "anti-steering statute." App. 103a.

Where the interest sought to be furthered by the restriction on interstate commerce "could be promoted as well with a lesser impact

(Continued...)

The core dispute in this case has consistently been whether *Exxon* establishes a *per se* rule that anti-vertical integration statutes are non-discriminatory, or whether *Exxon* requires application of a "business shifting" test to determine whether the statute's purpose or effect is to protect local independent firms from out-of-state, integrated ones. Intervenors claim there is "no circuit split about how to apply *Exxon*." Opp. 17. Their Opposition belies the assertion. Intervenors do not deny that other circuits (i) have recognized that *Exxon* requires a "business shifting" analysis, and (ii) have applied *Exxon* in invalidating facially-neutral statutes. Pet. 28 (citing cases applying *Exxon's* test). Nor can they deny that the Fifth Circuit disregarded *Exxon's* "business shifting" test. This is a direct circuit conflict.[2]

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on interstate activities," this Court has struck such bans under the *Pike* inquiry. *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970); *Lewis v. BT Inv. Managers, Inc.*, 447 U.S. 27, 43 (1980) ("outright prohibition on entry" by the targeted out-of-state bank was unjustifiable where less restrictive measures available).

The courts below made no analysis of less restrictive alternatives as part of their *Pike* reviews.

[2] Intervenors argue that HB 1131 does not fail *Exxon's* "business shifting" test because there was insufficient evidence that local body shops are the primary beneficiaries of the law. Opp. 6, 15. They are wrong. But that also begs the question of why the body shop Intervenors are here continuing their vigorous defense of HB 1131.

Intervenors' assertion of uncertain effect is controverted by the district court's factual findings that (i) there are "relatively few (about 5)" interstate firms, compared with approximately 4,600 local body shops; (ii) there was a 50% drop in Sterling's business following enactment of HB 1131; and (iii) the statute as passed was intended to "protect the interests of those [local] shops who participate in

(Continued...)

Intervenors denigrate *Exxon's* "business shifting" test as a "footnote," claiming the Court merely made a non-binding observation about discrimination. They emphasize the word "may" in the Court's statement about business shifting. Opp. 13. All that ignores that this Court in *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 194, 196 (1994), applied *Exxon's* "business shifting" test to invalidate a facially-neutral statute. Other courts have done so as well. Pet. 28.

Intervenors' floodgates argument – that state laws will be routinely struck down "any time the law causes *some* business to shift from interstate firms to intrastate firms," Opp. 13 (emphasis added) – blatantly misstates Allstate's and other courts' reading of *Exxon*. Under *Exxon*'s "business shifting" test, three elements must be satisfied:

(i) the burdened class must be disproportionately foreign,

(ii) the benefited class must be disproportionately local, and

(iii) the two classes must compete (i.e., must be "similarly situated"), causing business to shift disproportionately from the former to the latter.

---

Allstate's PRO program," which consists primarily of locally domiciled shops. App. 56a, 64a-65a, 100a.

Thus, a law that shifts business from out-of-state firms to local ones *may* – but does not *always* – have a discriminatory effect. It is not easy to meet all three facets of the test. But the test is a sensible delineator of discriminatory effect. Indeed, proper application of the "business shifting" test can explain the result in *every* Supreme Court and lower court decision, save this one.

### 3. Intervenors' Opposition Highlights The Need To Clarify When Firms Are "Similarly Situated."

Allstate explained that the Fifth Circuit's interpretation of whether favored and disfavored firms are "similarly situated" conflicts with the decisions of other circuits, which have applied this Court's competition test as set forth in *Bacchus, Gen. Motors Corp. v. Tracy*, 519 U.S. 278 (1997), and *United Haulers Ass'n, Inc. v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 127 S.Ct. 1786 (2007). Pet. 20-22. Intervenors do not and cannot deny that the Fifth Circuit ignored these cases. Nor do they deny that, under the competition test, Sterling and the local body shops are "similarly situated."

Rather, Intervenors argue that courts can declare, on a case-by-case basis, that firms are *ipso facto* dissimilarly situated. Opp. 18-19. For this, they cite *LensCrafters, Inc. v. Robinson*, 403 F.3d 798 (6th Cir. 2005), which viewed vertical integration as a "special case" not subject to the competition test. *Id.* at 804. Ironically, their

argument underscores the existence of a circuit split, calling for prompt resolution.[3]

### 4. Intervenors' Opposition Underscores The Need To Clarify Whether This Court's "Mixed Motives" Test Or The Fifth Circuit's "Primary Purpose" Test Controls.

Allstate demonstrated the conflict between the Fifth Circuit's "primary purpose" and this Court's "mixed motives" test. Pet. 15-17. Under the "primary purpose" test, heightened scrutiny is reserved for statutes primarily motivated by protectionist concerns. That approach conflicts with the way this Court has handled mixed-motive statutes, most notably those condemned in *Hunt* and *West Lynn Creamery*. Under those decisions, a substantial impermissible purpose triggers the heightened scrutiny by which any arguably permissible purpose is measured. *Id.*

Intervenors do not deny that the Fifth Circuit's "primary purpose" test conflicts with this Court's and other circuits' "mixed motives" test. Instead, they declare that this is not a "mixed motive" case.

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[3] Intervenors do not deny that, on the same facts addressed by the Sixth Circuit in *LensCrafters*, another lower court reach a directly contrary result. *Nat'l Ass'n of Optometrists & Opticians v. Lockyer*, 463 F. Supp. 2d 1116, 1129 (E.D.Cal. 2006) (expressly rejecting the Sixth (and the Fifth) Circuit's approach as inconsistent with *Tracy*). Intervenors say that, because the California case is currently on appeal, this Court should withhold review. But the lower court conflict is clear and direct. The two cases also illustrate how prevalent anti-Wal-Mart legislation is and the artful forms taken to protect local competitors from novel, interstate competition.

Opp. 12. That assertion was rejected below. The district court found that HB 1131 was "spurred by a coalition of small business owners who compete with ... Sterling," and that its purpose "was to protect one business model over another by favoring [overwhelmingly local] independent autobody shops over those [exclusively out-of-state competitors] owned by insurers." App. 79a, 80a. The Fifth Circuit agreed. App. 6a n.3. Indeed, the Fifth Circuit fashioned its "primary purpose" test because it was too "difficult to say . . . what primary factor motivated the passage of the legislation," since "both sides find passages ... supporting their view of the predominant reason." App. 6a.

Intervenors' snippets purporting to reflect a "consumer protection" purpose are irrelevant. At best, they show mixed motives. And their suggestion that the Fifth Circuit properly found HB 1131 non-discriminatory, based on the "totality of circumstances," Opp. 11-13, is a mere reformulation of that court's ginned-up "primary purpose" test. *See also* Pet. 25 (noting the lack of any, let alone credible, probative evidence of a pattern, practice, or policy of "cutting corners").

### 5. Intervenors' Opposition Confirms The Need For This Court's Guidance In Establishing Discriminatory Purpose.

Allstate explained the lower court confusion concerning how to determine discriminatory intent. Pet. 24-27 (noting conflict between the "objective observer standard" of *McCreary County v. Am. Civil Liberties Union of Ky.*, 545 U.S. 844, 862 (2005), and the Fifth Circuit's facial acceptance of the

Legislature's "official" pronouncements). This case presents an excellent vehicle for clarifying that this Court's "objective observer" test governs.

The Court's guidance is critically needed because the Fifth Circuit's "primary purpose" test is an open door to "ingenious" discrimination. *Best,* 311 U.S. at 455. That baleful result contradicts this Court's instruction in *Hunt*, namely that a legislature's benign motive "does not end the inquiry" since it "would mean that the Commerce Clause of itself imposes no limitations on state action ... save for the rare instance where a state artlessly discloses an avowed purpose to discriminate against interstate goods." 432 U.S. at 350 (internal citations and quotations omitted).

Under this Court's "mixed motives" jurisprudence, there is no need to for a court to decide which purpose – the legitimate or protectionist one – held greater sway over the hearts and minds of state legislators. Under the Fifth Circuit's "primary purpose" test, however, courts must engage in this difficult inquiry. That approach conflicts with settled methodology. *See* Pet. 16 n.2, 26-27 (citing *McCready's* "objective observer" standard and numerous Supreme Court Commerce Clause cases examining legislative intent).

Hence, it is all the more important for this Court to provide guidance as to what evidence courts may appropriately consider in determining legislative purpose. Intervenors confirm this need. They argue that courts should not even consider the statements of the elected officials who sponsored the legislation. In their view, "comments of individual legislators are

not controlling on the intent of the legislature as a whole." Opp. at 12 (citing *Chrysler Corp. v. Brown*, 441 U.S. 281, 311 (1979)). That is not the law. For one thing, *Chrysler* involved a question of statutory interpretation; it did not address how courts should determine whether a legislature acted with impermissible discriminatory intent.

More broadly, if statements of the legislative sponsors are irrelevant, then how can discriminatory intent be proven? Must the court accept the one-sentence, scrubbed statement of legislative intent, but disregard all other probative evidence? This Court has roundly eschewed such a rubber-stamp approach. Moreover, the protectionist rhetoric in the record – which is pervasive – is of the character this Court and lower courts have relied upon for decades in discerning discriminatory intent. *See* Pet. 24-27 (citing cases). In an age of growing protectionism, this is not the time to allow lower courts to abandon this Court's settled jurisprudential methodologies.

## CONCLUSION

For the foregoing reasons, this Court should grant the petition and reverse the decision of the Court of Appeals.

Respectfully submitted,

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January 22, 2008